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Remarks:

Executive Secretary
7/25/83
Date

3637 (10-81)

THE WHITE HOUSE
WASHINGTON

CABINET AFFAIRS STAFFING MEMORANDUM

DATE: 7/25/83 NUMBER: 118828CA DUE BY: _____

SUBJECT: Cabinet Council on Economic Affairs - July 26, 1983 - 8:45 am

In the Roosevelt Room

	ACTION	FYI
ALL CABINET MEMBERS	☐	☐
Vice President	☑	☐
State	☑	☐
Treasury	☑	☐
Defense	☑	☐
Attorney General	☐	☑
Interior	☐	☑
Agriculture	☑	☐
Commerce	☑	☐
Labor	☑	☐
HHS	☐	☑
HUD	☑	☐
Transportation	☑	☐
Energy	☐	☑
Education	☐	☑
Counsellor	☑	☐
OMB	☑	☐
CIA	☐	☑
UN	☐	☑
USTR	☑	☐
CEA	☑	☐
CEQ	☐	☐
OSTP	☐	☐
_____	☐	☐
_____	☐	☐

	ACTION	FYI
Baker	☑	☐
Deaver	☐	☐
Clark	☐	☑
Darman *(For WH Staffing)*	☑	☐
Harper	☑	☐
Jenkins	☐	☑
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CCCT/Gunn	☐	☐
CCEA/Porter	☑	☐
CCFA/Boggs	☐	☐
CCHR/Carleson	☐	☐
CCLP/Uhlmann	☐	☐
CCMA/Bledsoe	☐	☐
CCNRE/Boggs	☐	☐

REMARKS:

The Cabinet Council on Economic Affairs will meet on Tuesday, July 26, 1983 at 8:45 am in the Roosevelt Room. The agenda and background papers are enclosed.

RETURN TO:

☐ Craig L. Fuller
Assistant to the President
for Cabinet Affairs
456-2823

☑ Tom Gibson
Associate Director
Cabinet Affairs
456-2800

THE WHITE HOUSE

WASHINGTON

July 22, 1983

MEMORANDUM FOR THE CABINET COUNCIL ON ECONOMIC AFFAIRS

FROM: ROGER B. PORTER RBP

SUBJECT: Agenda and Papers for the July 26 Meeting

The agenda and papers for the July 26 meeting of the Cabinet Council on Economic Affairs are attached. The meeting is scheduled for 8:45 a.m. in the Roosevelt Room.

The first agenda item is conservation and renewable energy tax credits. As part of the fiscal year 1983 budget, the Administration proposed repealing all business energy tax subsidies and special provisions allowing states and localities to issue tax-exempt industrial development bonds to finance certain energy property, effective January 1, 1983. In response to this proposal, both Houses of Congress adopted resolutions supporting the energy tax credits. This year bills have been introduced in both houses to extend many of the credits through 1990 and the Department of the Treasury has indicated its opposition to such an extension.

The Department of Energy supports extension of the conservation and renewable energy tax credits and has requested that the Cabinet Council review this issue. An issue paper prepared by the Office of Policy Development working with the Departments of the Treasury and Energy and the Office of Management and Budget outlining the principal arguments for supporting and opposing such credits is attached.

The second agenda item is a continuation of the discussion on U.S. and EC agricultural policy differences. At the Council's July 5 meeting, Secretary Block presented a comparison of what the Department of Agriculture considered the major differences between U.S. and EC agricultural policies. He indicated that the Department would return to the Council in a few weeks with a followup presentation. A paper, prepared by the Department of Agriculture, on "U.S. Alternative Responses to the EC Common Agricultural Policy" is also attached.

Attachments

THE WHITE HOUSE

WASHINGTON

CABINET COUNCIL ON ECONOMIC AFFAIRS

July 26, 1983

8:45 a.m.

Roosevelt Room

AGENDA

1. Renewable Energy and Conservation Tax Credits (CM#390)
2. U.S. and EC Agricultural Policy Differences (CM#293)

July 22, 1983

CABINET COUNCIL ON ECONOMIC AFFAIRS

Issue Paper

Conservation and Renewable Energy Tax Credits

Background

In the Energy Tax Act of 1978 and the Crude Oil Windfall Profit Tax Act of 1980, a series of energy tax credits were enacted or modified to encourage investments in conservation and renewable energy technologies. The expiration date of the residential conservation and renewable tax credits and most of the business energy supply investment tax credits was set as December 31, 1985. The excise tax exemption for alcohol fuels was set as December 31, 1992. The business energy conservation tax credits and parts of the business energy supply investment tax credits expired December 31, 1982.

As part of the Fiscal Year 1983 Budget, the Administration proposed to repeal all business energy tax subsidies and to repeal special provisions allowing States and localities to issue tax-exempt industrial development bonds to finance certain energy property, effective January 1, 1983. In response to this proposal, both Houses of Congress adopted resolutions supporting the energy tax credits, with 265 Representatives and 63 Senators supporting the respective resolutions.

This year bills have been introduced in both Houses to extend many of the credits through 1990, increase the subsidy (e.g. from 25 percent to 35 percent for business credits) and expand their application (e.g. include passive solar).

The Department of the Treasury this year has twice indicated to Congress its opposition to extending the business energy tax credits; in June 17 testimony before the Senate Finance Committee, and in a July 12 written statement to the House Committee on Science and Technology.

The Department of Energy supports a five year extension of the business energy tax credits which expire in 1985, but not their expansion. Since November 1982, the Department of Energy has testified several times that it supports extension of the conservation and renewable energy tax credits.

A description of the existing tax credits for conservation and renewable energy sources is attached at Tab A.

Arguments for Permitting the Business Energy Tax Credits to Expire

At the time the energy tax incentives were enacted price controls and supply allocations were in effect on both crude oil and natural gas and there was substantial resistance to decontrol. Prices of both oil and natural gas paid by consumers were substantially below replacement costs, as reflected by the price of imported oil. Oil imports were growing at the same time that domestic consumption was being subsidized and domestic production discouraged.

Because of price controls, business firms had an insufficient incentive to invest in energy-conserving capital or in alternative energy sources (other than oil or gas), or to use alternative fuels, such as those derived from alcohol, wood, or biomass. In the absence of free market prices, an economic rationale existed for tax incentives for conservation and renewable energy.

- Since enactment of the credits, crude oil prices have been decontrolled and natural gas prices are being decontrolled under the National Gas Policy Act. As a result, the credits are no longer needed because most firms confront the true replacement cost of energy and therefore have sufficient incentive to invest in energy conservation and renewable energy and to purchase alternative fuels, without targeted tax incentives.

- Tax incentives for specific investments are inconsistent with the Administration's philosophy of relying on markets to allocate resources efficiently and determine patterns of energy use.

- The Accelerated Cost Recovery System (ACRS), enacted as part of the Economic Recovery Tax Act, has removed tax impediments to business investment -- including investments now eligible for energy tax incentives -- without dictating firms' choices among investment alternatives.

- The energy tax incentives distort the allocation of resources, encouraging firms to undertake investments that are uneconomic at current market prices, and to purchase higher cost fuels where a lower cost substitute is available. As a result, these incentives divert workers, capital, and initiative from more productive uses elsewhere in the economy and lower the net productivity of the capital stock.

- By reducing the cost of only some conservation measures, the incentives discourage other, potentially more efficient

approaches. New inventions and refinements in old technology not covered by the subsidy are at a disadvantage in the market when the Federal government interferes to subsidize the competition.

Arguments for Extending the Business Energy Tax Credits

The energy policy goal of this Adminstration is to allow market forces to work to provide adequate supplies of energy at reasonable prices in a manner that encourages a balanced energy system and preserves environmental quality. The goal requires that a consistent framework of Federal policies and programs be supported to provide for progress in the energy sector.

- The use of energy tax credits to stimulate increased conservation and renewable energy supports this goal by helping to reduce overall energy demand and by diversifying our sources of energy.

- The existence of the energy tax credits provided a useful part of the Administration's justification for reducing DOE spending on these technologies. For example, the Carter FY 1982 budget provided $1.7 billion for conservation and renewables programs, which was reduced to roughly $800 million after Congressional action on the Reagan budget revisions. To the extent that the Federal Government provides subsidies for conservation and renewables, it is preferable to do so through tax credits, which allow the marketplace to make investment decisions on the most effective technologies rather than through spending programs managed by the Federal Government.

- A number of economic factors have inhibited conservation and renewable energy development. The recent decline in energy prices, and energy prices anticipated through the late 1980's, have discouraged investments in high cost conservation and alternative energy technologies. In addition, high interest rates and a slow economy have further limited the penetration of new technologies. Many businesses in these emerging industries argue that they will simply fold unless conservation and renewable energy tax credits are extended.

- There has not been a predictable climate for investments in conservation and renewable energy projects.

  -- Current business tax credit statutes do not generally provide an affirmative commitment for long term renewable energy projects, terminating the credit for any ongoing projects on December 31, 1985. This date is too proximate to permit the tax credits for multi-year renewable energy investments to be effective.

-- Certain regulations for the tax credits enacted in 1978 were not provided until 1981, and a repeal of existing credits was proposed in 1982.

-- The Economic Recovery Tax Act of 1981 (ERTA) and the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) combined to increase uncertainty and confusion. 1982 TEFRA provisions substantially decreased the effective value of ACRS and thereby decreased the impact of existing renewable business tax credits.

-- Important provisions of Public Utility Regulatory Policies Act of 1978 (PURPA), dealing with cogeneration and small power producer interconnection with utilities, were resolved only last month by the Supreme Court.

o Energy tax credits available for an extended but limited period can expand demand for the affected products and stimulate future cost reductions that may permit businesses to survive and expand without continued tax incentives. The renewables industry alone estimates that it will grow from the current $3 billion to $7 billion annually by 1990, if tax credits are extended. Commercializing conservation and renewable energy technologies tends to be labor intensive and have a higher employment multiplier effect that alternative energy technologies.

o Investors supporting development of an entirely new industry, (such as renewable energy) require a "risk premium" reflected in the requirement of a higher rate of return (industry estimates that 75 percent of business renewable energy investments are made by third party investors with numerous investment options). The role of the tax credits is to provide the investors in relatively high risk projects the potential for reasonable rates of return.

o The revenue impacts of tax credits for conservation and renewable energy currently represent less than a fifth of total tax credits available for energy developers. (Expensing of intangible drilling costs and the depletion allowance for oil, gas and minerals will continue to result in three times the revenue loss as conservation and renewables tax credits extend into the future. There is no expiration date on these credits.)

o Regardless of any economic drawbacks the credits may have, they are politically popular. By supporting extension of the credits, the Administration may be better able to shape the final tax credit legislation and avoid a difficult legislative fight.

Evidence on the Effectiveness of the Credits

- Studies of the effect of the tax credits on investor decision-making offer mixed conclusions. For example:

  -- A March 1982 GAO study concluded that information available at that time on the effect of the tax credits was inconclusive. A March 1983 GAO study of 4 selected solar and wind energy projects concluded that 2 of the projects would still be viable in the absence of the tax credits, although the sponsors claimed that they could not obtain private financing without them.

  -- A Booz-Allen and Hamilton Study concludes that without energy investment tax credits, solar and wind technologies will remain generally uncompetitive. However if the existing 15 percent investment tax credit were continued beyond 1985, significant penetration of these technologies is likely to result.

Conservation and Renewable Energy Tax Credits

Federal Tax Credits

The following is a summary of existing conservation and renewable energy tax credits:

Business Energy Conservation Investment Tax Credits (Expired December 31, 1982)

Provides a 10 percent nonrefundable investment tax credit for specially defined energy properties. These include heat exchangers, regenerators, heat wheels, recuperating waste heat boilers, heat pipes, turbulators, preheaters, combustable gas recovery systems, automatic energy control systems, economizers, energy saving modifications to aluminum electrolytic cells, recycling equipment, vans used for carpools and certain cogeneration equipment. These tax credits expired December 31, 1982 unless taxpayer had entered into binding contracts to acquire at least 50 percent of the total estimated value of the investment as well as having applied for related permits, etc., on or before December 31, 1982.

Intercity Bus Investment Tax Credit (Expires December 31, 1985)

Provides a 10 percent nonrefundable investment tax credit for qualified intercity buses that increase the operating seating capacity of a firm over the previous year of operation.

Business Energy Supply Investment Tax Credits (Group A - Expired December 31, 1982)

Provides a 10 percent nonrefundable tax credit for equipment using (burning) energy besides oil or natural gas or equipment used to provide synthetic fuel from substances other than oil or natural gas or to extract oil and natural gas from shale rock or geopressurized brine respectively.

Business Energy Supply Investment Tax Credits (Group B - Expires December 31, 1985)

These credits are in addition to the regular 10 percent investment tax credit, thus the total investment credit for firms purchasing qualified energy property varies in most cases from 20 to 25 percent of the cost of the equipment.

Provides a 15 percent nonrefundable investment tax credit for equipment which uses solar or wind energy for heating, cooling, hot water, process heat or electrical production; for equipment

related to geothermal or ocean thermal energy or the use of biomass to produce energy. Up to an 11 percent nonrefundable credit is available for small scale hydroelectric generating plants and equipment. As the size of such facilities increases, the 11 percent credit is reduced until at 125 megawatts capacity no credit is available.

Residential Energy Conservation Credit (Expires December 31, 1985)

Provides a 15 percent nonrefundable tax credit to homeowners or renters for purchases of approved residential conservation investments up to a limit of $300 of total credit. Approved investments include insulation, caulking and weatherstripping, stormdoors and windows, ignition systems that replace gas pilot lights, automatic thermostats and energy use meters. Credits are not available for houses that were not completed before April 20, 1977 or if the conservation investment was financed by a tax-exempt bond.

Residential Renewable Energy Supply Credit (Expires December 31, 1985)

Provides a 40 percent nonrefundable investment tax credit for up to $10,000 of renewable energy source equipment that provides heating, cooling, hot water or electricity in a household.

Exemption of Federal Motorfuel Excise Taxes for Gasohol and the Alcohol Fuel Tax Credit (Expires December 31, 1992)

An exemption of 5 ¢ per gallon of Federal motor fuel excise tax is provided for motor fuels which contains at least 10 percent alcohol. In addition, a 40 ¢ per gallon (for 150-190 proof) or a 50 ¢ per gallon (for 190-200 proof) tax credit is available for alcohol which is used as a fuel for internal combustion engines and is not used in gasohol blends which receive the Federal excise tax exemption.

Alternative Fuel Production Credit (Expires December 31, 1999)

Provides a $3.00 per barrel of oil equivalent tax credit for alternative fuels. Except for process wood fuels, steam produced from solid agricultural by-products, and gas produced from Devonian shale, the full credit is only available if the price of oil is at or below $23 per barrel, and the credit phases out entirely when it reaches $29.50 per barrel. (In addition, other restrictions apply to this $3 per barrel tax credit).

Special Tax Treatment of State and Local Industrial Bonds for Energy Production Facilities (No Expiration Date)

Exempts Federal taxation of interest on Industrial Development Bonds used to finance small scale State or local government

hydroelectric facilities of less than 25 megawatts capacity (25-125 megawatt facilities eligible for partial tax exempt financing), facilities owned by a state or local government which produce steam or alcohol from solid waste, and certain state operated renewable energy programs.

Table 1
Revenue Loss Due to Energy Tax Expenditures*
(millions of dollars)
Fiscal Year

	1982	1983	1984	1985
Conservation and Renewable Energy				
Business Energy Conservation Credits	232	137	33	14
Credit for Intercity Buses	**	**	**	**
Business Supply Energy Credits				
Group A	23	41	30	17
Group B	194	173	172	160
Residential Energy Conservation Credits	359	328	304	304
Residential Energy Supply Credits	251	341	451	610
Alcohol Fuel Credit	58	85	95	109
Alternative Fuel Production Credit	15	40	70	93
Special Tax Treatment of State and Local IDCs for Energy Production Facilities	6	15	21	27
Total	1,138	1,160	1,176	1,334
Expensing of Intangible Drilling Costs	3,400	1,500	1,200	NA
Percentage of Depletion Allowance	2,100	1,850	1,700	NA

* Source: U.S. Treasury, unpublished data.

** Revenue loss for intercity bus credit included with estimate of revenue loss for Business Energy Conservation Credits.

DEPARTMENT OF AGRICULTURE
OFFICE OF THE SECRETARY
WASHINGTON, D. C. 20250

July 22, 1983

MEMORANDUM FOR THE CABINET COUNCIL ON ECONOMIC AFFAIRS

FROM: JOHN R. BLOCK JRB

SUBJECT: U.S. Alternative Responses To The European Community's Common Agricultural Policy

U.S.-EC agricultural trade relations have slipped to a post-war low over the last 2 years as slowed growth in world trade increased competition for the export markets both need to keep their farm programs viable and their agriculture sectors healthy. To date, the EC has successfully used export subsidies to expand its share of the stagnant world market and to transfer the drop in exports, prices, and incomes resulting from the trade slowdown to other exporters, particularly the U.S.

Given prospects for slowed growth in trade for the next several years, the U.S. will have to choose between pressing the EC for changes in its export subsidy program or loosing more of its export market share. Pressing the EC for reform aggressively enough to be effective risks a U.S.-EC trade war, but further losses in U.S. exports will worsen the depressed situation in the farm sector and prolong costly government intervention in agriculture.

Intensified U.S.-EC Competition for World Markets

The slowdown in agricultural trade experienced since 1981 has increased competition for markets and undermined relations among the major exporters--particularly between the U.S. and the EC. Both grew dependent on trade over the 1970's to ease their domestic farm problems. Export growth allowed the U.S. to cut back on costly acreage and income programs and the EC to dispose of mounting surpluses--albeit with the help of export subsidies.

The situation has changed radically. Economic recession, policy retrenchment in importing countries, and good crops generally slowed growth in trade from 4-5 % per year during the 1970's to less than 1.5 % since 1980.

U.S. and EC adjustments to this trade slowdown differed sharply. The U.S. has borne most of the pressure on farm prices, incomes, and government program expenses due to its direct link to the world market and its weakened competitive position caused by an appreciating dollar. Commodity prices have fallen a quarter, farm incomes have dropped a third, and government expenditures have increased eight-fold since 1980. Sharp cutbacks in production are being made and sizeable stocks have been built-up.

The EC, on the other hand, has responded to the slowdown by raising export subsidies enough to prevent any drop off in exports and or adjustment in farm prices, incomes, and production levels. Subsidies in 1983 are likely

to reach $9 billion on sales of possibly $31 billion. This exacerbates the adjustment problems of the other exporters, particularly the U.S. While difficult to measure precisely, the EC's subsidies have displaced possibly $5-6 billion in U.S. farm exports annually since 1980. The EC's isolation of its farm sector from market adjustments has also destabilized world prices and, in turn, U.S. farm incomes, prices, and government payments.

Alternative U.S. Policy Responses

Several basic policy stances are open to the U.S. to win EC modification of the most damaging of its policies.

The U.S. could wait out the current trade slump and depend on economic recovery and exchange rate adjustments to revive U.S. farm exports later in the 1980's. The U.S. would continue to pressure the EC for trade policy reform in GATT but with little expectation of success.

In its favor, such a stance would defuse the current confrontation and protect U.S.-EC interests outside agriculture. However, it would also require considerable farm sector adjustment. To balance supply and demand, farm prices would have to be allowed to drop to even lower levels or the U.S. Treasury would have to sustain added expenditures of possibly $3-4 billion per year to restrain production. The agricultural sector would face EC export displacement of up to $8 billion per year by the later half of the decade. Equally important, the U.S. would continue to be the residual adjustor to widening fluctuations in world supply and demand.

Rather than waiting it out, the U.S. could also take a more aggressive stance designed win EC export subsidy reform through budget pressure. The resources available to the EC to fund Community activities are fixed by cumbersome treaty arrangements. While these resources have been more than adequate in the past, growth in export subsidies has pushed EC spending to within $800 million, or 3 percent, of its funding limit.

A U.S. limited confrontation stance would involve using aggressive export marketing--including subsidies--to threaten the EC with the loss of key dairy, poultry, and grain product markets. The pressure generated could be considerable as the EC faced substantially higher expenses either in the form of the added subsidies needed to maintain their exports or the higher domestic program costs incurred if displaced exports were kept at home but reform postponed.

In its favor, a limited confrontation would increase the budget pressure on the EC to reform substantially. Moreover, targeting the U.S. initiative to strategic products and markets would help to minimize the cost of the confrontation to the U.S. However, short-term Community budget fixes appear far more likely than the basic reforms sought by the U.S.

Moreover, while the EC is vulnerable in many areas such as dairy, a U.S. initiative would have to include other products that do not lend themselves to a confrontation in order to generate any significant amount of budget pressure. In such a setting, the U.S. could invest $1.4-1.6 billion to threaten the EC with $800-900 million in added subsidy cost or the loss of $1.6 billion in exports.

Hence, a limited confrontation could well prove both costly and ineffective--possibly counter-productive if it discredited the internal EC reform movement interested in the basic policy changes sought by the U.S.

The U.S. options also include an open confrontation stance that assumes budget pressure is still the most effective tool available to lobby for EC reform but that pressure would have to be substantially greater to force the issue. To bring this increased pressure to bear and protect U.S. markets from EC retaliation, the U.S. would have to shift to large-scale subsidization of a broader range of products to all buyers. In this

open confrontation, U.S. imports of EC farm products--particularly wine and spirits and dairy products--would also be severely curtailed.

These activities in combination would involve $3-$6 billion in U.S. expense annually for possibly 1-3 years. The initiative would threaten the Community with export losses of $4-5 billion and up to $2 billion in increased CAP costs due to the added expense involved in disposing of displaced exports internally.

In its favor, such a stance would force the EC into reform. The budget costs involved in maintaining the current Community system would quite likely be too great. Internal stocking and disposal arrangements would likely be made in the short term while basic farm and trade policy reforms were worked out in the longer run.

However, such a stance could prove extremely costly to the U.S. and counter productive in terms of the reforms it generated in the EC. The U.S. would finally have forced the reform issue, but the reforms undertaken by the EC could well aim at closing CAP loopholes and damaging U.S. trade interests rather than liberalizing trade. These actions would not change the Community's basic agricultural problem but would relieve the internal budget pressure building for the more basic reforms. In this setting, the U.S. initiative might well give the EC's program new life and postpone ultimate resolution of the reform issue for several years. It would also disrupt the world trading system, damage the interests of allies such as New Zealand, and subsidize purchases by countries such as the USSR.

While unlikely, given the EC's interest in confining any confrontation to agriculture, the Community could also respond to an open confrontation by expanding the conflict to areas outside agriculture.

U.S. options to deal with the trade problem also include modification of domestic farm programs. At issue here is how to use domestic farm programs--particularly price support programs--to ensure that U.S. farm products are priced as competitively on the world market as possible. Maximizing competitiveness puts the U.S. in a stronger position to win and hold export markets without subsidies and is consistent with long-standing U.S. trade policies. More competitive pricing of U.S. products also increases the cost of the subsidies necessary to move EC products on the market without requiring actions targeted directly against the EC.

This alternative goes beyond addressing the relatively narrow question of competition with the EC for world markets and deals with the more basic problem of the farm sector's excess capacity. It assumes that high and rising support levels exacerbate the surplus problem generated by dampened growth in export demand, the above average yields experienced so far in the 1980's, and the rapid appreciation of the dollar.

The initiatives possible here include lowering of support for individual products with the most pronounced support problems--wheat and dairy--as well as sector-wide adjustments designed to offset a general upward drift in support levels. However, such a stance would require considerable adjustment in farm incomes and resource use.

An Eclectic U.S. Strategy

No one of these initiatives alone appears likely to resolve the U.S.-EC confrontation. Elements of all four can be used to develop a strategy to resolve both the short term export subsidy problem while working in the longer run to improve the operation of the world market.

Critical to resolving the conflict is the recognition in the U.S. and the EC that farm export expectations have to be scaled back over at least the next several years. This recognition will force both the U.S. and the EC to search for alternative policies to deal with their farm problems. The U.S. has already moved aggressively in this area with acreage reduction programs. However, some effective means of reining in output in the EC and winning export subsidy reform has yet to be found.

Given the unsuccessful conclusion of extensive multilateral and bilateral consultations with the EC, any significant change in the EC's programs appears to depend on far more aggressive U.S. initiatives including:

- Targeting selected EC export markets--such as the Egyptian flour or Saudi Arabian poultry markets--for subsidized sales of U.S. products as a means of stressing our committment to winning changes in the Community's export subsidy policy. Each action will be designed to increase the cost of the EC program and would be accompanied by a strong statement that government interference in the market process is a losing proposition and that we prefer a market-oriented policy. The targets would be chosen on the basis of recent relative U.S.-EC market share changes, use of EC subsidies, least cost to the U.S. Treasury, and least possible disruption of non-subsidizing interests.

- Reducing U.S. commodity support levels to accomplish a number of objectives. Lower loan rates will make our producers more sensitive to changes in the market and our products more price-competitive internationally while reducing the incentive for other suppliers to expand output. This step will increase the cost to the EC of their export subsidy program and worsen an already difficult EC budget situation.

- Take advantage of every opportunity in the media and in public forums to bring the message to the European consumer/taxpayer of the cost of the CAP--cost in terms of budget outlay, of food prices relative to the

U.S. and in international tension as the Community moves further from a market oriented agriculture. The U.S. would also take every opportunity in bilateral and multilateral forums to increase consensus among other countries of benefits of open markets, thereby increasing the number of other countries pressuring the EC.

Critical in assuring that the short term resolution of the export subsidy problem worked in the longer term to improve operation of the world market is convincing the EC of the merits of its functioning as a full and responsible partner in the world market.